Supreme Court, U.S.
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No. 95-1943

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1995

In re WILKER S. CONNER and JANICE M. CONNER,

Debtors.

JOHN D. BARKLEY, TRUSTEE,

Petitioner,

vs.

WILKER S. and JANICE M. CONNER, ORTHOPEDIC CLINIC, 401K PROFIT SHARING PLAN, and TRUST AGREEMENT, PUREGO COMPANY,

Respondents.

REPLY TO OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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PETITIONER'S REPLY

I. SUMMARY OF THE REPLY

The Debtor has unrestricted access to portions of her Pension Plan in spite of the Plan's anti-alienation clause. The Trustee, standing in the shoes of the Debtor, has the same power to withdraw those funds. Because the Debtor can withdraw these funds at any time and for any reason, the Trustee should be allowed to withdraw these funds and make them part of the bankruptcy estate. The Debtor should not be allowed to keep from creditors the money to which the Debtor had complete access simply because other portions of the plan are restricted and ERISA qualified.

II. CORRECTION OF RESPONDENTS' MISSTATEMENTS IN THE OPPOSITION.

Respondents' Opposition to the Petition contains several factual and legal misstatements, which Petitioner notes and corrects as follows:

A. Petitioner has consistently challenged whether the unrestricted after-tax account is a legitimate component of Debtor's ERISA qualified pension plan.

Respondents argue that because Petitioner conceded that the Debtor's Pension Plan is "ERISA qualified" the Court

need not consider the definition of "ERISA Qualified." Opposition, p. 12. Although Petitioner conceded in the courts below that Debtor's Pension Plan is "ERISA qualified," the real issue, which Petitioner has consistently challenged, is whether the after-tax account is a legitimately and appropriately restricted beneficial interest such that it should be covered by the ERISA qualification and thus not become property of the Debtor's bankruptcy estate. The Debtor recognized this controverted issue at the Ninth Circuit. See Appellee's Ninth Circuit Opening Brief, p. 20 ("the Trustee does question the exclusion of the After-Tax Account"); Appellant's BAP Opening Brief, p. 6 ("The After-Tax Account of the Plan does not include any restriction as to the Debtor's access to the monies in that account").

Respondents' emphasis on the Plan's ERISA qualification distracts from the real issue: whether an after-tax account which is not restricted as required under 11 U.S.C. § 541(c)(2) and fails the second prong of the Court's decision in Patterson v. Schumate, 504 U.S. 753, 112 S. Ct. 2242 (1992), should be protected in bankruptcy simply because it is part of an otherwise qualified ERISA pension plan.

To resolve this question, the Court needs to address the extent of the restrictions imposed by § 541(c)(2), e.g., whether unrestricted access to some pension plan funds by

the debtor nevertheless satisfies the mandate that an ERISA qualified plan contain a "restriction on the transfer of a beneficial interest" pursuant to 11 U.S.C. § 541(c)(2) and the Court's Shumate decision. The Petitioner is not attempting to challenge the legitimacy of the Debtor's overall pension plan; instead, Petitioner seeks a determination of the effect of the Debtor's unrestricted access to a portion of the pension plan funds with respect to § 541(c)(2).

Respondents assert without authority that "if the Plan is ERISA qualified..., then all of the Plan accounts necessarily are as well." Opposition, p. 14. The reason Respondents cite no authority is that none exists. Shumate never examined an ERISA qualified plan containing unrestricted "accounts." As outlined in the Petition, courts have interpreted the debtor's unrestricted access to pension benefits quite differently with dramatically inconsistent results. See Petition, p. 25. If the Ninth Circuit's decision stands, individuals will be allowed to withdraw significant sums of money from certain accounts within their "qualified" pension plans "for any reason and at any time" and yet prohibit their creditors from obtaining those same funds by filing bankruptcy. The individual has

unrestricted access to these "pension" plan accounts before bankruptcy and then absolute protection from creditors' access to these funds after bankruptcy. This result clearly does not fulfill the literal restriction requirements of § 541(c)(2) as required by the Court's Shumate decision in spite of the fact that the Plan at issue is ERISA qualified.

B. The after-tax account is a separate account, capable of isolation and analysis.

Respondents incorrectly assert that the undisputed record establishes that the after-tax account is not a separate account and cannot be isolated for analysis. Opposition, p. 9. Respondents themselves identify three distinct bookkeeping subaccounts, one of which is called the "After-Tax Account" that contains approximately $38,000 and accrues interest distinct from the "Pre-Tax Account" and the "Employer Account."

Respondents have shown their ability to identify the source and amounts in each account. In fact, the Plan under § 8.8(A) entitled, "Withdrawals of Accounts During Employment," states that withdrawals may be made from the voluntary contributions up to "the value of his After-Tax Account on the date of withdrawal...." Petition, p. A119.

Contrary to Respondent's claim, the Plan administrators are not only capable of distinguishing the separate after-tax account within the Plan, but are required to do so when the individual makes a withdrawal from the after- tax account.

C. ERISA and IRS anti-alienation rules are not limited to third-party transactions.

Respondents argue, without authority, that the anti-alienation provisions of 29 U.S.C. § 1056(d)(2) and 26 U.S.C. § 401(a)(13) are not designed to prevent plan participants from accessing plan funds. Opposition, p. 18. Respondents argue that the only purpose for an anti-alienation provision is to protect funds against third-party creditors. Id. Respondents are simply wrong.

In I.R.S. Revenue Ruling 89-14, 1989-1 C.B. 111, a plan participant borrowed money from the pension plan at an unreasonably low interest rate. The Revenue Ruling held that the arrangement was an assignment and alienation of benefits to the participant in violation of § 401(a)(13) because the accrued nonforfeitable benefits were used as security for the loan at an unreasonably low rate of interest.

As discussed in the Petition, § 1056(d)(2) suggests by negative implication that a withdrawal from the plan by a

participant can be treated as an alienation and assignment: "a loan made to a participant ... shall not be treated as an assignment or alienation if such loan is secured by the participant's accrued nonforfeitable benefit and is exempt from the tax imposed by" sections of the Internal Revenue Code. 29 U.S.C. § 1056(d)(2).

Based on the Revenue Ruling and the language of the ERISA statute cited above, Respondents are incorrect in their assertion that plan participants can be the recipients of an assignment or alienation of benefits without violating the express provisions of ERISA and/or the I.R.C.

D. The Plan Agreement itself allows unrestricted withdrawal of after-tax contributions.

Respondents imply that only the Plan Summary and not the Plan Agreement allow unrestricted access to the after-tax account. Opposition, p. 9. Respondents are wrong. Petitioner relies on the Plan Summary because it more clearly explains the unrestricted nature of the after-tax account. However, the Plan Agreement itself expressly states the unrestricted nature of the after-tax account:

> A Participant who is Employed may withdraw amounts from his Voluntary Account provided

> that (1) the aggregate amounts withdrawn shall not exceed the greater of (a) the aggregate amount of his After-Tax Contributions, and (b) the value of his After-Tax Account on the date of withdrawal and (2) Participant's spouse must consent in writing....

Plan Document § 8.8(A), Petition, A119. This section contains no hardship requirement as required for withdrawal from the pre-tax account under § 8.8(B).

The Agreement says, in the words of the Plan Summary, that after-tax contributions may be withdrawn "for any reason and at any time." The unrestricted nature of the after-tax account was recognized by Judge Jones of the Ninth Circuit BAP in his concurring opinion when he states that "it is undisputed that the Debtor has access to the funds in the after-tax account at any time and for any reason." In re Corner, 165 B.R. 901, 904 (9th Cir. BAP 1994) (Jones, J., concurring). Judge Jones stated that this unrestricted account should, in his opinion, have been included in the property of the Debtor's estate, however, he was powerless to reverse the Ninth Circuit's decision in In re Reuter, 11 F.3d 850 (9th Cir. 1993), that bound him to a contrary result.

E. Respondents rely on exhibits that were not part of the record below and should not be considered by the Court.

Respondents submit two letters from the Internal Revenue Service in their Opposition which were not introduced in the lower courts. These exhibits should be excluded from consideration. First Nat. Bank of North East v. Fockler, 649 F.3d 213, 215-216 (5th Cir. 1981) (appellate court cannot consider materials outside the record).

II. REPLY TO OPPOSITION ARGUMENT

A. This Court has Jurisdiction pursuant to Rule 10(c).

Rule 10(c) of the Rules of the Supreme Court of the United States sets forth the compelling reasons for this Court's assertion of jurisdiction including "a United States court of appeals has decided an important question of federal law that has not been, but should be, settled by this Court, or has decided an important federal question in a way that conflicts with relevant decisions of this Court."

Both of these jurisdictional bases are applicable in this case because this Court has not resolved the issue of an

"ERISA qualified" pension plan containing unrestricted accounts and because the Ninth Circuit did not properly apply the Shumate test to the unrestricted account in the Debtor's pension plan. Without resolution of this issue uncertainty will continue in the administration of the increasing number of bankruptcies that involve pension plans. Likewise, leaving the Ninth Circuit's decision in this case to remain will lead other appellate and bankruptcy courts to decisions that are inconsistent with the Shumate decision.

B. The Ninth Circuit's decision in Reuter is inconsistent with the Court's decision in Shumate.

Respondents continue to rely on the Ninth Circuit's decision in Reuter. The Reuter court stated that the only issue for its determination was whether the plan contains an anti-alienation clause sufficient to satisfy ERISA, regardless of whether any part of the pension plan funds are wholly unrestricted. This analysis only satisfies the first prong of this Court's decision in Shumate.

Judge Jones of the Ninth Circuit BAP in his concurring opinion recognized the need to apply Shumate's second prong. Although he felt compelled to follow Reuter, 11 F.2d 850, as controlling law in the Ninth Circuit, Judge Jones

stated that "it is undisputed that the Debtor has access to the funds in the after-tax account at any time and for any reason. Therefore, the Debtor may be unable to satisfy the second prong of the Shumate analysis which entails subjecting the anti-alienation provision to scrutiny under section 541(c)(2)." In re Connor, 165 B.R. 901 at 904 (9th Cir. BAP 1994) (Jones, J., concurring.) In reality, there is absolutely no restriction on the after-tax account. As discussed above, § 8.8(A) of the Plan allows for unrestricted access to the after-tax account in spite of the anti-alienation provision.

If a plan can be deemed ERISA qualified based on the existence of an anti-alienation provision, but in reality allow unrestricted access to particular funds, the intent of § 541(c)(2) is thwarted. Application of this Court's second prong in Shumate eliminates precisely this problem. Unfortunately, the Ninth Circuit has decided to ignore this second prong of the Shumate decision. By interpreting "ERISA qualified" broadly without any further analysis, the Ninth Circuit has circumvented the Court's two-prong test.

IV. CONCLUSION.

The Court should REVERSE the Ninth Circuit's decision in this case, and determine that a Debtor's unrestricted access to pension plan funds does not satisfy the requirements of 11 U.S.C. § 541(c)(2).

Respectfully submitted,

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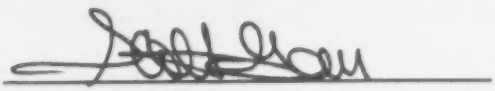
By 

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